MICC INVESTMENTS LIMITED

1978 ANNUAL REPORT

Si vous désirez recevoir ce rapport en français, veuillez vous adresser au :

Secrétaire

Les Placements MICC, Limitee
C.P. 14, 401 rue Bay, chambre 1200
Toronto, Ontario M5H 2Y4

MICC Investments Limited is a public company whose shares are listed on the Toronto and Montreal stock exchanges. As at December 31, 1978 over 97% of its outstanding common shares were held by shareholders of record with addresses in Canada. Its principal operating subsidiary is The Mortgage Insurance Company of Canada (MICC).

MICC was incorporated by Act of Parliament passed in December 1963 and commenced operations in June 1964. It is licensed and operates in each of the provinces. MICC's activities fall under the jurisdiction of the Federal Department of Insurance whose staff carry out regular inspections and whose approval is obtained for all insurance programs.

MICC is engaged in the business of providing financial guarantees in the real estate market. Under its first mortgage program, protection is provided to mortgage lenders and investors against losses on mortgage loans covering houses (including condominium units), rental projects, commercial and industrial properties and vacation homes. The Company also insures second mortgages on houses and income properties. MICC also offers a lease guarantee program under which lessors of commercial and industrial real estate are insured against loss through failure of a tenant to pay rent. In addition, MICC insures the New Home Warranty Programs in Ontario and Quebec for their obligation to reimburse homeowners against loss of deposit and cost of major structural repairs to homes. MICC also provides an inspection and appraisal service for a fee to mortgage lenders.

MICC now has over 13 years' experience and has developed a staff highly skilled in mortgage underwriting. More than 400 mortgage lenders use its services, including most major financial institutions in Canada.

MICC Investments Limited and
The Mortgage Insurance Company of Canada
Board of Directors
(as at February 28, 1979)

Robert A. Bandeen, President and Chief Executive Officer Canadian National Railway Company, Montreal, Quebec

Michel F. Belanger, President and Chief Executive Officer The Provincial Bank of Canada Montreal, Quebec

R. C. Brown, Partner Blake, Cassels & Graydon, Toronto, Ontario

John Cochran, President Domtar Construction Materials, Montreal, Quebec

H. Reuben Cohen, Q.C. Barrister & Solicitor Moncton, New Brunswick

***Harold Corrigan,** President Alcan Canada Products Limited, Toronto, Ontario

***S. E. Eagles,** Chairman, President and Chief Executive Officer Marathon Realty Company Limited, Toronto, Ontario

***Gardner English,** President Kopas & Burritt Funding Inc. Toronto, Ontario

Peter Kilburn, Honorary Chairman Greenshields Incorporated, Montreal, Quebec

***Raymond Lavoie,** President and Chief Executive Officer Credit Foncier-Franco Canadien, Montreal, Quebec

R. M. MacIntosh, Executive Vice-President The Bank of Nova Scotia, Toronto, Ontario

George S. May, Chief Executive Officer, Canadian Co-operative Credit Society Limited, Toronto, Ontario

***Fred H. McNeil,** Chairman Bank of Montreal, Montreal, Quebec

***Reginald T. Ryan,** President MICC Investments Limited, Toronto, Ontario

Ralph T. Scurfield, President Nu-West Development Corporation Ltd., Calgary, Alberta

G. D. Sutton, President Canadian Enterprise Development Corporation Limited, Toronto, Ontario

G. J. van den Berg, Company Director, Beaconsfield, Quebec

***B. G. Willis,** Executive Vice-President, Greenshields Incorporated, Toronto, Ontario

MICC Investments Limited
Executive Officers

Reginald T. Ryan, President

David C. Toms, Vice-President Finance and Secretary

The Mortgage Insurance Company of Canada
Executive Officers

Reginald T. Ryan, President

James McAvoy, Senior Vice-President

David C. Toms, Vice-President Finance and Secretary

Georges W. Carpentier, Vice-President and Chief Underwriter

*Member of the Executive Committee of MICC Investments Limited

Highlights for the year

	1978	1977	Increase
	$	$	%
Premiums Written	44,385,022	33,203,376	33.7
Underwriting Revenue	20,940,074	15,182,940	37.9
Investment Income	22,331,224	16,714,769	33.6
Losses on Claims Incurred	20,578,726	8,809,506	133.6
Net Earnings	13,562,759	14,758,462	(8.1)
Net Earnings Available to Common Shareholders	9,513,086	12,537,592	(24.1)
Total Assets	307,834,175	221,755,996	38.9
Shareholders' Equity	161,775,422	106,659,291	51.7

Earnings Per Common Share	$ 1.66	$ 2.19	(24.2)
Earnings Per Common Share (fully diluted)	$ 1.65	$ 2.19	(24.7)
Common Dividends Paid	$ .56	$ .37¼	50.3

President's Report to Shareholders

Despite lackluster economic conditions in many parts of the country, 1978 was a very active one for the Company. The Mortgage Insurance Company of Canada, the Company's principal subsidiary, achieved another record year for new mortgage insurance business. MICC improved its market share (based on total mortgages approved by lending institutions) from approximately 22% in 1977 to 30% in 1978. Potential premiums from business committed under Canadian mortgage insurance and lease guarantee programs totalled $58,750,408, an increase of 36% over the 1977 figure of $43,024,254. Net premiums written amounted to $44,385,022 compared to $33,203,376 in 1977, an increase of 34%. At year end Canadian mortgage insurance in force was $10.7 billion compared to $8.4 billion at December 31, 1977, and liability under the lease guarantee program was $50 million compared to $31 million at the end of 1977. Details are set out in the Review of Operations, page 14.

The high level of unemployment combined with a flat housing market in many areas of Canada resulted in a substantial increase in losses on claims during 1978 and a reduction in earnings. Net earnings for the year totalled $13,562,759 compared with $14,758,462 for 1977 equal to $1.65 per common share compared with $2.19 in 1977, both on a fully diluted basis.

Claim losses increased from $8,809,506 in 1977 to $20,578,726 in 1978. Losses last year rose to 98% of underwriting revenue compared to 58% in 1977.

During the year, MICC's staff worked diligently with approved lenders and correspondents to improve mortgage collection and claims procedures. In addition, more restrictive underwriting criteria were introduced for certain programs. While the ratio of insured mortgages in default remained fairly constant throughout the year, the proportion of defaults, resulting in claims has increased. Top priority is being given to defaults, claims and the handling of real estate acquired on payment of claims to make these operations as efficient as possible with a view to minimizing losses to the Company. However, we do not foresee any

immediate upward movement in housing prices generally or any significant decrease in unemployment and therefore we do not look for improvement in losses in 1979. A detailed analysis of defaults, claims and real estate will be found on pages 22 & 23.

Early in 1979, application fee increases were introduced to bring processing fees more in line with our costs. In addition, a modest number of premium increases were put into effect based primarily on our claims experience.

Our investment portfolio performed well again in 1978. The portfolio increased to $269,139,761 at year end from $200,935,733 at December 31, 1977. The net after tax return on investment decreased slightly from 7.18% in 1977 to 7% in 1978. The value of securities held, in relation to cost, improved considerably again this year. Details of the investment portfolio of the insurance company are contained on page 19.

During the year, the Company raised $45 million in new capital by way of two public issues. In the spring, we completed an issue of $25 million of 8⅝% cumulative, redeemable preferred shares, Series C, and last November we issued $20 million of 8% cumulative, redeemable, convertible second preferred shares, Series A. Although it appears that capital now available will be adequate to support new business written in 1979, company policy is to obtain new capital well in advance of needs and it is likely, therefore, we will be seeking new capital in 1979.

During the year, the Company paid $4,049,673 in regular dividends to preferred shareholders. Dividends on the common shares were increased 2¢ per share per quarter, rising from 11¢ for the first quarter to 17¢ per share paid for the final quarter.

New housing starts in Canada in 1978 fell to 227,667 units from 245,724 in 1977. This reduced level of activity should help to correct an excess supply situation in a number of communities resulting from over building in previous years. While the Alberta market was still strong, most other parts of the country were experiencing problems. The result was that real estate prices were fairly stable throughout the year and it continued to be a buyer's market.

While the 1979 economic outlook for Canada points to a subdued pace of growth by the standards of the past, there are encouraging indications of improvement in several aspects of our domestic economic performance. It is expected that we will achieve a lower average rate of inflation than the 9% increase of last year. Domestic industry should continue to reap benefits from the lower dollar. Capital spending prospects are cautiously better after several years of weakness. However, it is likely that the unemployment rate will begin to rise again, reversing the gently declining trend of 1978. With respect to housing, we see a slightly lower level of starts than was achieved last year. Mortgage funds should be in ample supply but, interest rates will be at higher levels, at least for the first half of the year.

Based on a record carryover of potential premiums from new business committed, but not funded, in 1978, and on our expectations for new business to be committed this year, we anticipate that net premiums written will be at a high level again in 1979. We also expect that we will be called upon to settle a substantial number of claims from lenders this year. Of course, this is what mortgage insurance is all about and we are pleased that we were able to protect our lender clients in 1978 from losses that they would have taken had their mortgages not been covered by our insurance. Over the years, since the Company commenced operations in 1964, substantial reserves have been built up from premiums received from lenders. These reserves are more than adequate to meet the current level of losses. The cumulative losses incurred by the Company from 1964 to the end of 1978 represent 57.7% of premiums earned during that period.

At last year's Annual Meeting, we welcomed to our Board of Directors three new members – Mr. Michel Belanger, Mr. Reuben Cohen and Mr. George May. These gentlemen are making an important contribution to the affairs of your Company. At this year's Annual Meeting, Mr. Peter Kilburn will be retiring from the Board of Directors. Mr. Kilburn was an original member of the Board and I would like to record sincere appreciation for his valuable contribution to the affairs of the Company and its subsidiary over the past fifteen years.

During 1978, our staff increased considerably in numbers and were again called upon to carry a heavy load. I would like to thank each one of them sincerely for their dedication and effort during the past year.

R. T. Ryan
President
MICC Investments Limited

MICC Investments Limited

Consolidated Balance Sheet

as at December 31, 1978

Assets	**1978**	1977
	$	$
Cash and accounts receivable		
Cash	**751,890**	1,702,841
Interest accrued and sundry receivables	**4,287,611**	2,295,896
Premiums receivable	**3,072,860**	2,641,727
Income taxes recoverable	**—**	1,267,470
Foreign income taxes recoverable	**532,990**	106,596
Due from reinsurers	**293,700**	24,114
	8,939,051	8,038,644
Real Estate	**26,772,514**	11,632,805
Investments		
Treasury bills and other short-term securities — at cost	**32,597,425**	25,111,390
Bonds and debentures — at amortized value (market value $66,961,485; 1977 — $62,082,782)	**70,622,207**	63,480,227
Preferred stocks — at market value (cost $88,079,206; 1977 — $62,582,856)	**91,297,019**	66,989,074
Common stocks — at market value (cost $54,705,157; 1977 — $37,077,235)	**67,518,668**	42,129,339
Mortgages — at amortized value	**7,104,442**	2,700,503
Charlotte Properties Limited	**—**	525,200
	269,139,761	200,935,733
Other Assets		
Loan to trustees under employee stock purchase plan (Note 6)	**130,973**	188,449
Other	**554,663**	244,208
Capital expense — at amortized cost (Notes 3 and 4)	**2,297,213**	716,157
	2,982,849	1,148,814
	307,834,175	221,755,996

Signed on behalf of the Board

R. T. Ryan, Director

B. G. Willis, Director

Liabilities	1978	1977
	$	$
Accounts Payable		
Due to reinsurers	**24,735**	103,624
Provision for claims	**10,003,141**	4,974,415
Accounts payable and accrued liabilities	**1,190,434**	981,617
Interest payable on income debentures	**204,603**	175,178
Premium taxes payable	**986,024**	444,962
Income taxes payable	**925,957**	—
Due for securities purchased	**160,711**	2,650,435
	13,495,605	9,330,231
Other Liabilities		
Deferred revenue (Note 2)	**106,724,839**	82,486,553
Deferred income taxes	**10,838,309**	8,279,921
Income debentures (Note 3)	**15,000,000**	15,000,000
	132,563,148	105,766,474
	146,058,753	115,096,705
Shareholders' Equity		
Capital Stock (Note 4)	**105,793,803**	61,861,563
Retained Earnings (Note 5)	**43,776,907**	37,588,498
	149,570,710	99,450,061
Unrealized Gain on Stocks	**12,204,712**	7,209,230
	161,775,422	106,659,291
	307,834,175	221,755,996

MICC Investments Limited

Consolidated Statement of Earnings

For the Year Ended December 31, 1978

	1978	1977
	$	$
Revenue		
Net premiums written	44,385,022	33,203,376
Application fees	2,833,775	2,264,609
Commission income	5,391	16,844
Inspection service and appraisal fees	314,717	88,864
	47,538,905	35,573,693
Less: Increase in deferred revenue	26,598,831	20,390,753
Underwriting revenue	20,940,074	15,182,940
Investment income		
Interest and amortization	8,645,755	5,762,009
Dividends	9,652,705	8,710,841
Realized gain on disposal of investments	3,420,198	1,772,393
Other (Note 7)	612,566	469,526
	22,331,224	16,714,769
	43,271,298	31,897,709
Expenses		
Insurance underwriting and policy issuance expenses	4,694,638	3,094,069
Premium taxes	1,024,101	772,037
	5,718,739	3,866,106
Less: Increase in deferred expenses	2,223,961	966,627
	3,494,778	2,899,479
Losses on claims incurred	20,578,726	8,809,506
Other operating expenses	2,556,146	1,616,272
Income debenture interest and amortization expense (Note 3)	1,157,145	983,610
	27,786,795	14,308,867
Earnings Before Income Taxes	15,484,503	17,588,842
Provision for Income Taxes		
Current	977,004	1,354,120
Deferred	944,740	1,476,260
	1,921,744	2,830,380
Net Earnings for the Year	13,562,759	14,758,462
Earnings per Common Share		
Basic earnings per share	$1.66	$2.19
Fully diluted earnings per share	$1.65	$2.19
Weighted daily average number of common shares outstanding	5,719,680	5,715,805

MICC Investments Limited

Consolidated Statement of Unrealized Gain on Stocks

For the Year Ended December 31, 1978

	1978	1977
	$	$
Unrealized Gain on Stocks		
Beginning of year	**7,209,230**	1,380,161
Unrealized gain on stocks for the year	**6,573,002**	8,028,161
	13,782,232	9,408,322
Deferred income taxes	**1,577,520**	2,199,092
Unrealized Gain on Stocks		
End of year	**12,204,712**	7,209,230

Consolidated Statement of Retained Earnings

For the Year Ended December 31, 1978

	1978	1977
	$	$
Retained Earnings		
Beginning of year	**37,588,498**	27,273,508
Net earnings for the year	**13,562,759**	14,758,462
	51,151,257	42,031,970
Amortization of capital expenses, less related income taxes (Note 4)	**113,286**	92,794
Expenses on purchase of preferred shares	**8,370**	670
Cash dividends –		
Preferred	**4,049,673**	2,220,870
Common	**3,203,021**	2,129,138
	7,374,350	4,443,472
Retained Earnings		
End of Year	**43,776,907**	37,588,498

MICC Investments Limited

Consolidated Statement of Changes in Financial Position

For the Year Ended December 31, 1978

	1978	1977
Source of Funds	**$**	$
Operations —		
Net earnings for the year	**13,562,759**	14,758,462
Increase in net deferred revenue (Note 2)	**24,238,286**	19,561,725
Income taxes deferred	**944,740**	1,456,038
Depreciation and amortization	**173,321**	101,829
Funds generated from operations	**38,919,106**	35,878,054
Common shares issued	**32,240**	31,374
Preferred shares issued (net of expenses)	**43,240,006**	4,951,495
Debentures issued (net of expenses)	**—**	4,951,045
Increase in accounts payable	**4,165,374**	4,904,027
Decrease in loan to trustees under employee stock purchase plan	**57,476**	46,016
Other	**59,512**	20,222
	86,473,714	50,782,233
Use of Funds		
Increase in real estate	**15,139,709**	7,270,385
Increase in cash and accounts receivable	**900,407**	3,903,763
Purchase of fixed assets	**458,248**	143,649
Dividends —		
Preferred shares	**4,049,673**	2,220,870
Common shares	**3,203,021**	2,129,138
Purchase of preferred shares	**1,091,630**	130,670
	24,842,688	15,798,475
Funds Available for Investment	**61,631,026**	34,983,758
Investment Funds — Beginning of Year	**200,935,733**	157,923,814
	262,566,759	192,907,572
Unrealized gain on stocks for the year	**6,573,002**	8,028,161
Investment Funds — End of Year	**269,139,761**	200,935,733

MICC Investments Limited

Notes to Consolidated Financial Statements

For the year ended December 31, 1978

1. Accounting Policies

The accounts of MICC are included herein in accordance with generally accepted accounting principles. The application of these principles is set out for the following significant items:

Principles of consolidation

The consolidated financial statements of MICC Investments Limited (the "Company") include the accounts of its subsidiaries, Charlotte Properties Limited, previously carried at cost, and The Mortgage Insurance Company of Canada ("MICC").

Premiums

Net premiums written are deferred and then taken into underwriting revenue as earned over the life of the related policies. Prior to 1974, the majority of policies were written for a term of fifteen years; since then the majority of policies have been written for twenty years. The rate or formula under which premiums are earned relates to the amount of risk in each year of coverage.

Application fees and commission income

Application fees received on insurance policies written and commission income received on reinsurance premiums ceded to a reinsurer are taken into income as received.

Underwriting and policy issuance expenses and premium taxes

Underwriting and policy issuance expenses and premium taxes in excess of application fees and commission income are deferred and then amortized against premiums as the premiums are earned.

Losses on claims incurred

Losses on claims incurred represents the difference between the amounts claimed by insureds and estimated recoveries from the sale of real estate. Provisions for losses are made when it is apparent that defaults by borrowers will result in claims. An additional provision, based on past experience, is also made on other loans in default.

Investment income

(a) Treasury bills and other short-term securities – Interest is recorded as income as it accrues. Realized gains and losses are taken into income.

(b) Bonds, debentures and mortgages – Interest is recorded as income as it accrues. The premium or discount between cost and maturity value is amortized into income over the period to maturity. A gain or loss on the sale of a bond, debenture or mortgage is deferred and then amortized over the term to maturity of the security sold.

(c) Stocks – Dividends are recorded as income on the ex-dividend date. Gains and losses on disposal of stocks are taken into income when realized. Unrealized gains and losses on stocks are accounted for in a special statement (consolidated statement of unrealized gain on stocks), the balance of which is transferred to shareholders' equity.

Real estate

Real estate is carried in the accounts at its estimated realizable value after deduction of real estate commission and other sales related expenses.

2. Deferred Revenue

Deferred revenue consists of deferred premiums, after deduction of deferred underwriting and policy issuance expenses and premium taxes.

3. Income Debentures

Income debentures consist of three series. Series A and B, in amounts of $2,000,000 and $8,000,000 respectively, mature on September 30, 1981 with mandatory prepayment as to 33.4% on September 30, 1979 and 33.33% on September 30, 1980. Series C in the amount of $5,000,000 matures on March 31, 1985 with mandatory prepayment as to 33.34% on March 31, 1983 and March 31, 1984. Interest is payable at the rate of 8¼% on Series A debentures, at 50% of the prime bank rate, plus 2.5% on Series B debentures and at 7½% on Series C debentures. Interest on these debentures is not deductible in computing taxable income.

Costs incurred in connection with these issues have been capitalized and are being amortized against earnings on a straight-line basis over the terms of the debentures. As at December 31, 1978, unamortized capital expenses relating to income debentures amounted to $68,152.

4. Capital Stock

Under a Certificate of Continuance dated April 17, 1978, existing preferred shares were redesignated first preferred shares and a new class of second preferred shares issuable in series was created. In addition, the limitation of the number of authorized common shares was removed.

The authorized, issued and fully paid capital stock of the company consists of:

	1978	1977
	$	$
Authorized		
3,951,600 (1977 – 3,976,000) first preferred shares issuable in series		
Unlimited (1977 – nil) second preferred shares issuable in series		
Unlimited (1977 – 10,000,000) common shares without par value		
Issued and fully paid		
752,000 (1977 – 776,000) 10% first preferred shares Series A	**18,800,000**	19,400,000
200,000 (1977 – 200,000) 7¾% first preferred shares Series B	**5,000,000**	5,000,000
980,000 (1977 – nil) 8⅝% first preferred shares Series C	**24,500,000**	—
800,000 (1977 – nil) 8% second preferred shares Series A	**20,000,000**	—
5,719,680 (1977 – 5,715,805) common shares	**37,493,803**	37,461,563
	105,793,803	61,861,563

(a) PREFERRED SHARES

(i) First preferred shares Series A

800,000 of first preferred shares were issued as 10% cumulative redeemable first preferred shares Series A, of which 752,000 were outstanding at December 31, 1978.

The 10% cumulative redeemable preferred shares Series A are subject to mandatory sinking fund redemption at par for:

(i) 24,000 shares on March 15 in each of the years 1978 to 1981 inclusive;

(ii) 56,000 shares on March 15 in each of the years 1982 to 1986 inclusive; and

(iii) 72,000 shares on March 15, 1987 and each year thereafter.

Commencing March 15, 1982 the company may increase any annual sinking fund by 24,000 shares. The company is entitled to anticipate sinking fund requirements by purchasing shares in the market at prices not exceeding the redemption price. Subsequent to March 15, 1981 the company may redeem shares not required for sinking fund purposes at a premium of 5%, declining annually thereafter to par value on March 15, 1986.

During 1978 the company acquired 24,000 preferred shares Series A to meet sinking fund requirements to March 15, 1978.

(ii) First preferred shares Series B

200,000 of first preferred shares were issued as 7¾% cumulative redeemable first preferred shares Series B, all of which were outstanding at December 31, 1978.

The 7¾% cumulative redeemable preferred shares Series B are subject to mandatory sinking fund redemption at par for 66,800 shares on March 31, 1983 and 66,600 shares on March 31, 1984 and March 31, 1985.

The company is entitled to anticipate sinking fund requirements by purchasing shares in the market at prices not exceeding the redemption price. Subsequent to March 31, 1982 the company may redeem shares not required for sinking fund purposes at a premium of 3%, declining annually thereafter to par value on March 31, 1985.

(iii) First preferred shares Series C

During 1978, 1,000,000 of first preferred shares were issued as 8⅝% first preferred shares Series C for a cash consideration of $25,000,000.

The first preferred shares Series C are non-redeemable prior to March 31, 1983 and are subject to a purchase fund under which the company shall make all reasonable efforts to purchase 10,000 shares in each calendar quarter, beginning with the calendar quarter ending September 30, 1978, at a price not exceeding $25 plus cost of purchase. This obligation is cumulative from quarter to quarter but to the extent not satisfied on December 31 of each calendar year, is extinguished. Subsequent to March 30, 1983, the company may redeem shares not required for purchase fund purposes at a premium of 5%, declining annually thereafter to par value on April 1, 1988.

During 1978, the company acquired 20,000 first preferred shares Series C to meet 1978 purchase fund requirements.

(iv) Second preferred shares Series A

During 1978, 800,000 of second preferred shares were issued as 8% cumulative redeemable convertible second preferred shares Series A for a cash consideration of $20,000,000.

The second preferred shares Series A are non-redeemable prior to December 31, 1983 and are subject to a purchase fund under which the company shall make all reasonable efforts to purchase in each calendar quarter, commencing with the calendar quarter ending March 31, 1984, 0.75% of the difference between the number of second preferred shares Series A originally issued and the number of shares converted prior to such calendar quarter at a price not exceeding $25 per share plus costs of purchase. This obligation is cumulative from quarter to quarter, but to the extent not satisfied on December 31 of each calendar year, is extinguished. Subsequent to December 30, 1983 the company may redeem shares not required for purchase fund purposes at a premium of 5%, declining annually thereafter to par value on December 31, 1988.

The second preferred shares Series A are convertible on or before December 31, 1988 into fully paid common shares, at the holder's option, at a conversion price of $11.50 per common share on the basis of 2.173 common shares for each second preferred share held.

Costs incurred in connection with the issuance of preferred shares have been capitalized and are being amortized against retained earnings over the estimated term of the shares on a weighted average basis. As at December 31, 1978, unamortized capital expenses

relating to preferred shares amounted to $2,229,061.

(b) COMMON SHARES

During 1978, 3,875 common shares were issued for a cash consideration of $32,240 under the employee stock purchase plan.

A non-assignable stock option for the purchase of 10,000 common shares is held by a director of the company, and is exercisable until December 31, 1980 at a price of $9.00 per share.

5. Retained Earnings

Retained earnings includes an amount of $10,714,495, representing an appropriation of retained earnings in MICC as required by the Department of Insurance. This amount is not available for distribution to shareholders.

6. Employee Stock Purchase Plan

Loans made to two officers, one of whom is also a director, under the employee stock purchase plan, amounted to $48,518 as of December 31, 1978.

7. Foreign Exchange

Accounts in United States dollars have been translated in the following manner. Assets, being bonds, and liabilities, being primarily deferred revenue, have been translated at historical rates. Earnings have been translated into Canadian dollars at the average rate prevailing through the year.

The foreign exchange gain is reflected in the statement of earnings under other investment income (1978 gain – $254,066; 1977 gain – $469,526).

8. Comparative Figures

Certain items on the 1977 statement of earnings have been reclassified for comparative purposes.

Auditors' Report to the Shareholders

We have examined the consolidated balance sheet of MICC Investments Limited as at December 31, 1978 and the consolidated statements of earnings, retained earnings, unrealized gain on stocks and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1978 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Coopers & Lybrand
Chartered Accountants

February 9th, 1979

Transfer Agents

First Preferred Shares
National Trust Company, Limited

Second Preferred Shares
The Canada Trust Company

Common Shares
The Canada Trust Company

Registrars

First Preferred Shares
National Trust Company, Limited

Second Preferred Shares
The Canada Trust Company

Common Shares
Canada Permanent Trust Company

Auditors

Coopers & Lybrand

Review of Operations

New Business – Mortgage Insurance

First Mortgages

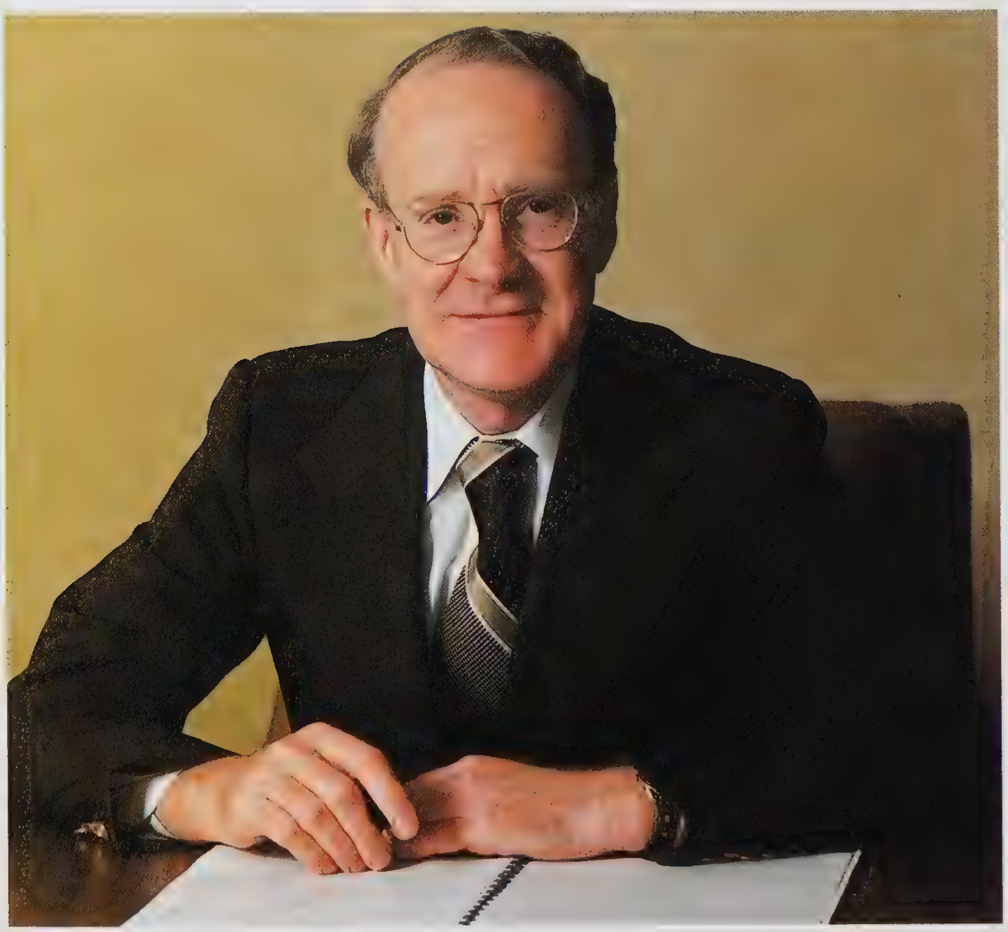
A record for new business was achieved last year with the issue of commitments to insure totalling $4.950 billion. When compared with 1977, this represents an increase of 36.2%. Underwriting statistics are detailed on page 21.

Commitments on mortgages for new and existing houses totalled $3.745 billion, of which $1.656 billion covered new construction and $2.068 billion existing housing. Each category showed increases over 1977, 45% for new properties and 34% for existing housing.

Commitments to insure mortgages on income producing properties increased from $950 million in 1977 to $1.250 billion in 1978 – residential rental (apartments and town housing) produced $623 million, an increase of 21%, while commercial-industrial commitments increased to $582 million, representing an increase of 34% over 1977. Total commitments for vacation homes showed a substantial increase, from $7 million in 1977 to $22 million, an increase of 198%.

The average insured high ratio house loan (for both new and existing homes) on a per unit basis amounted to $41,533 in 1978 compared to $38,559 the previous year. The average loan on new existing housing was $49,934 and $36,407 per unit respectively.

The average house loan, while showing a slight increase over the preceding year, is at a level which indicates that our services are utilized primarily for transactions in the moderate to medium price range.



J. McAvoy, Senior Vice-President

Second Mortgages

The volume of second mortgage business shows an increase of 225% over 1977 ; however, these programs still contribute nominally to total premiums written. Details are shown on page 21.

Lease Guarantee Insurance

During the year, 161 lease guarantee commitments were issued, for an aggregate insured rent of $49.4 million, compared to 145 commitments for an aggregate insured rent of $33.8 million in 1977. While premiums written declined marginally to $1,263,901 from $1,270,998 in 1977, the year ended with a substantial number of commitments still outstanding, representing $1,362,588 in potential premiums.

New Home Warranty Insurance

Premiums earned under the Ontario and Quebec New Home Warranty Programs amounted to $362,818 compared to $182,112 in 1977. Losses incurred under the Programs amounted to $272,114 compared to $136,584 in 1977. Amounts paid to the Ontario Program in 1978 exceeded the loss figure, but the excess is recoverable from the Program under the terms of the insurance agreement.

Potential Premiums

Total potential premium for all programs amounted to $59.650 million for the year 1978. This represents an increase of $15.138 million or 34% over 1977. As at December 31, 1978, commitments to insure in an amount of $3.033 billion, with a potential premium of $34.439 million, were outstanding. It should be noted, however, that 20%-25% of the commitments issued are cancelled or lapse and do not materialize into premiums written.

Comparison figures for the years 1977 and 1978 are shown in the table which follows.

Potential Premium	**1978**	1977
First Mortgages	**$**	$
Homeownership loans		
High-ratio	**31,554,070**	23,113,487
75% and less	**3,488,005**	2,037,947
Rental loans		
High-ratio	**8,556,932**	6,569,143
75% and less	**410,014**	579,982
Commercial/Industrial loans		
High-ratio	**8,335,873**	5,563,863
75% and less	**3,439,309**	3,316,295
Vacation Home loans	**378,963**	137,598
Second Mortgages		
Homeownership loans	**163,548**	94,262
Rental	**890**	—
Commercial/Industrial	**75,323**	15,898
Lease Guarantee Insurance	**2,347,481**	1,595,779
Condominium Deposit Insurance	**—**	37,002
New Home Warranty Insurance	**900,000**	1,453,006
Total Potential Premium	**59,650,408**	44,514,262

Left to Right
D. C. Toms, Vice-President Finance and Secretary
G. W. Carpentier, Vice-President and Chief Underwriter

Underwriting Policy

In the face of a less than buoyant economy and higher than normal inventories of housing and commercial and industrial properties in many parts of the country, the underwriting policy of the Company has been under continuous scrutiny during the past year. A strong effort has been made to keep abreast of local conditions to ensure that underwriting criteria are revised as required to ensure proper risk selection. Claims experience has been used as the basis for some adjustments to avoid situations that have been demonstrated to be less than satisfactory as investments for lenders or as risks for insurers. This focus on improving quality of new business will continue to be emphasized in 1979.

Approved Lenders and Correspondents

The Company added 73 new lender clients during the year. At year end there were 425 Approved Lenders and 57 Approved Correspondents. The Approved Lenders' list includes 11 chartered banks, 49 life insurance companies, 57 trust companies, 42 loan companies, 236 credit unions and caisses populaires, and 30 other type institutions.

Regional Offices

A new office was opened in Hamilton in 1978. MICC now has a total of 13 regional offices across the country, improving still further service to its lenders. A complete listing of offices will be found on page 24.

Services to Lenders

During the year 35,103 construction inspections were carried out on new properties. Appraisals were performed on 2,304 properties for lenders to assist them in their mortgage lending operations.

Defaults

The default ratio on all insured accounts remained relatively constant during the year. At December 31, 1978, 2,754 accounts were reported by lenders as being in default, for a default ratio of 0.96%, the same ratio as at the end of 1977. A provision for loss has been recorded and charged against income for many of these loans. While it appears that defaults have levelled off, we have noted that a greater percentage of defaults are now resulting in claims.

Top Row (left to right)
F. D. Teatro, Director, Administration and Personnel
D. S. Oxley, Investment Officer
J. D. H. Bergeron, Corporate Solicitor

Bottom Row (left to right)
C. Renaud, Director, Business Development
J. D. Hewitt, Director, Corporate Planning
A. D. Munro, Director, Claims and Real Estate

Losses on Claims Incurred

Losses on claims incurred on mortgage insurance increased significantly in 1978 to $19.7 million from $8.4 million in 1977. It should be noted that losses are estimated and charged to income at the earliest point in time that a loss is anticipated even though many months may pass before an actual claim is made and subsequently paid

Losses on insured house loans represented 78% of losses incurred during 1978, which is not surprising as this is the area in which we have been most active. A high proportion – i.e. 94% – of the losses occur in years 2-6 of a policy with 40% of the 1978 losses occurring in the 3rd year after a mortgage has been insured. Average loss on a high ratio house loan was approximately $9,200 last year.

It is difficult to identify all of the reasons for mortgage defaults. However, reports from lenders indicate that the major factors are high unemployment and a poor economy in many parts of the country, marital difficulties and a shortfall in actual earnings achieved by borrowers as compared to anticipated earnings.

Losses on claims incurred in the lease guarantee program increased from $160,679 in 1977 to $560,443 in 1978 This again, we believe, is a reflection of current economic conditions. However, we have noted a moderation in losses recently and if this continues, the level of claims should not continue to increase in 1979.

Real Estate

During the year 742 properties were acquired in settlement of claims for a total appraised value of $30,698,875 compared to 251 properties with a value of $12,204,485 in 1977. While the number of houses in inventory increased from 147 at the end of 1977 to 392 with a value of $12,094,294 at December 31, 1978, the rate of sale improved during the year and in the fourth quarter we sold more houses than we acquired. In some cases, and frequently for income properties, real estate acquired is withheld from the market while repairs or renovations are

carried out, level of occupancy is increased or the market improves. As at year end, MICC was holding 31 properties with a value of $1,021,500 off the market. It is expected that a number of these properties will be offered for sale in 1979.

During the year 489 parcels of real estate were sold for a total consideration of $18,138,797.

Under certain circumstances where an insured mortgage is in default, we have takenan assignment of the mortgage from the approved lender to take direct control of the legal process. At the end of the year we held 17 such mortgages which are carried at the underlying value of the real estate which amounted to $1,587,379.

Financial

At December 31, 1978, statutory accounting practices of property and casualty insurers were amended to confirm, in the main, with generally accepted accounting principles. Therefore, it was felt that it was no longer necessary to include the statutory balance sheet of the company in this Report.

During the year the company's parent subscribed for a further 500,000 preferred shares, increasing the issued capital of the company to $90,814,500 with total shareholders' equity now amounting to $156,560,693 compared with $100,199,962 at December 31, 1977 restated in accordance with generally accepted accounting principles.

Investments

During 1978 the investment strategy maintained a continued emphasis on high quality and liquidity due to the prevailing uncertain economic and market conditions. As the year progressed, interest rates rose and a gradual shift was made from liquid assets to Government of Canada bonds with 3 to 5-year term. This can be seen from the table below which indicates that long bonds increased from 4.7% of the portfolio in 1977 to 17.7% in 1978. At year-end 1978, 23% of the portfolio was held in cash and liquid assets.

Equity investments were modestly increased in both the preferred and common stockholdings. The increase in and turnover of these holdings emphasized both high quality and improvement of yield. At year-end equity investments represented 59.3% of the portfolio compared with 56.8% in 1977.

Due to both the impact of a higher cash liquid position during the year and to the lower yields available in the market, the net after-tax investment income, expressed as a percentage of the average portfolio, decreased slightly to 7% from 7.18% in 1977. The market value of the investment portfolio was 106.6% of cost at year-end 1978, compared to 107.2% as at December 31, 1977.

The following table shows a classification of the portfolio.

Classification	Cost 12/31/78	% of Total 1978	1977
	$		
Cash	1,408,000	0.6	0.9
Federal Government	43,633,025	18.1	32.4
Money Market	10,247,000	4.3	5.2
Cash and Liquid Assets	55,288,025	23.0	38.5
Long Bonds	42,735,253	17.7	4.7
Term Preferred	9,997,264	4.2	11.8
Sinking Fund Preferred	31,878,491	13.2	15.6
Conventional Preferred	32,849,854	13.6	2.5
Straight Preferred	74,725,609	31.0	29.9
Convertible Preferred	13,353,597	5.6	5.8
Common Stock	54,705,157	22.7	21.1
Common and Convertible Pfd	68,058,754	28.3	26.9
Total Equity	142,784,363	59.3	56.8
	240,807,641	100.0	100.0

MICC Investments Limited

Historical financial summary (Note 1)

	1978	1977	1976	1975	1974
MICC Investments Limited					
Premiums written	**$ 44,385,022**	33,203,376	20,177,102	19,552,099	19,515,633
Premiums earned	**$ 17,786,191**	12,812,623	9,845,571	8,294,195	6,326,450
Application fees and other	**$ 3,153,883**	2,370,317	1,481,468	1,357,518	1,346,505
Underwriting revenue	**$ 20,940,074**	15,182,940	11,327,039	9,651,713	7,672,955
Investment income	**$ 22,331,224**	16,714,769	12,359,676	7,939,314	5,192,680
Claims losses	**$ 20,578,726**	8,809,506	3,990,855	2,842,978	848,962
as a % of underwriting revenue	**98.27%**	58.02%	35.23%	29.5%	11.1%
Expenses	**$ 7,208,069**	5,499,361	3,996,588	3,146,856	2,606,484
as a % of premiums written	**16.24%**	16.56%	19.81%	16.09%	13.36%
Net earnings	**$ 13,562,759**	14,758,462	11,937,134	8,119,645	5,695,089
Shares outstanding (average)	**$ 5,719,680**	5,715,805	5,711,080	5,711,080	5,056,575
Earnings per share	**$ 1.66**	2.19	1.83	1.42	1.13
Total Assets	**$307,989,218**	221,755,996	167,560,020	124,981,531	88,836,756
Return on total assets	**5.12%**	7.58%	8.16%	7.59%	7.36%
Shareholders' Equity	**$161,775,422**	106,659,291	85,613,858	51,927,505	43,175,428
Return on common shareholders' equity	**10.83%**	16.90%	17.70%	17.08%	15.07%
Net after tax investment income expressed as a % of average investment portfolio (Note 2)	**7.00%**	7.18%	7.29%	6.98%	5.63%
The Mortgage Insurance Company of Canada					
Policyholders' reserves	**$123,322,031**	94,763,336	72,171,304	59,513,671	46,421,936
Capital	**$142,158,433**	95,199,064	83,712,795	61,396,071	43,096,140
Total capital and reserves	**$265,480,464**	189,962,400	155,884,099	120,909,742	89,518,076

Note: 1. Certain figures have been restated from those shown in previous annual reports to reflect current reporting procedures.

2. The investment portfolio does not include mortgages, and investment income excludes realized gains on disposal of equities.

The Mortgage Insurance Company of Canada
Underwriting statistics

	1978	1977	1976	1975	1974
Approved lenders and correspondents					
Lenders	**425**	352	279	234	180
Correspondents	**57**	58	52	60	50
Total	**482**	410	331	294	230
Commitments to insure issued (Canadian business)(1)			(,000 omitted)		
Mortgage Insurance					
First Mortgage Insurance Programs					
Homeownership Loans	**$**	$	$	$	$
High-Ratio	**3,183,407**	2,349,001	1,528,189	1,447,704	1,484,782
75% and less	**540,148**	336,340	348,030	282,611	112,093
Rental Loans					
High-Ratio	**580,810**	456,095	233,347	226,254	163,007
75% and less	**41,929**	59,906	21,189	25,935	7,462
Commercial/Industrial Loans					
High-Ratio	**361,490**	237,330	121,622	121,193	107,010
75% and less	**220,526**	196,668	142,343	105,526	81,451
Vacation Home Loans	**21,690**	7,273	5,725	8,751	3,870
Total	**4,950,000**	3,642,613	2,400,445	2,217,974	1,959,675
Second Mortgage Insurance Program					
Homeownership Loans	**$**	$	$	$	$
High-Ratio	**4,598**	1,903	1,361	—	—
75% and less	**941**	1,234	1,207	—	—
Income Properties (rental and comm./ind.)	**5,333**	200	—	—	—
Total	**10,872**	3,337	2,568	—	—
Lease Guarantee Program	**49,440**	33,799	33,214	24,237	17,902
Total Potential Premium(2)	**59,650**	44,514	27,786	25,442	22,303
Average Loans					
Homeownership Loans (High-Ratio)	**$**	$	$	$	$
New Construction (per unit)	**49,602**	45,635	42,342	38,647	34,270
Existing Homes (per unit)	**39,396**	34,399	30,275	28,118	24,341
Rental Projects (per loan)	**191,553**	170,375	148,157	157,000	134,689
Commercial/Industrial (per loan)	**305,039**	359,590	319,916	310,100	326,072
Vacation Homes (per unit)	**33,472**	21,412	26,615	24,578	17,162
GDS and TDS ratios	**%**	%	%	%	%
Gross Debt Service Ratio(3)	**23.9**	23.9	24.8	24.5	23.9
Total Debt Service Ratio(4)	**30.1**	29.7	30.3	30.1	29.2
Insurance in force	**$**	$	$	$	$
(Canadian Mortgage Insurance) At Year End (In Billions of Dollars)	**10.7**	8.4	7.0	5.7	3.6

Notes: (1) **Commitment Figures** are expressed in Gross Terms.
(2) **The Potential Premium Figure** represents the total premiums from all programs including new home warranty insurance (1978 $900,000).
(3) **GDS Ratio** (Gross Debt Service Ratio) – the percentage of gross income used for mortgage payments and property taxes
(4) **TDS Ratio** (Total Debt Service Ratio) – the percentage of gross income used for mortgage payments, property taxes and all other instalment debts.

Defaults and claims

Default Ratios	1978	1977	1976	1975	1974
	%	%	%	%	%
First Mortgage Insurance Programs					
Homeownership Loans					
High-Ratio	**0.95**	1.02	0.68	0.72	0.38
75% and less	**0.71**	0.56	0.26	0.23	—
Rental Loans	**1.36**	0.95	0.86	0.52	1.59
Commercial and Industrial Loans	**1.85**	1.57	0.85	0.75	0.19
Vacation Home Loans	**2.39**	1.05	0.31	—	—
Second Mortgage Insurance Programs	**0.53**	0.49	—	—	—
Overall Default Ratio	**0.96**	0.96	0.64	0.67	0.23

Claims Losses					
	$	$	$	$	$
First Mortgage Insurance Programs			(,000 omitted)		
Homeownership Loans					
High-Ratio	**14,502**	4,929	1,719	568	53
75% and less	**846**	72	52	—	—
Rental Loans	**2,890**	2,448	671	1,057	179
Commercial and Industrial Loans	**1,437**	966	1,068	139	7
Vacation Home Loans	**18**	—	—	—	—
Second Mortgage Loans	**38**	—	—	—	—
Total Mortgage Insurance Losses from Canadian Operations	**19,731**	8,414	3,510	1,764	239
Lease Guarantee Insurance Losses	**560**	161	83	22	20
New Home Warranty	**272**	137	—	—	—
U.S. Reinsurance Losses	**15**	98	398	1,057	590
Total claims losses	**20,579**	8,810	3,991	2,843	849

MICC Investments Limited

Real Estate

Real Estate Activity	Single Family		Rental		Commercial and Industrial		Total	
	No.	Book value	No.	Book value	No.	Book value	No.	Book value
		$		$		$		$
Held at December 31, 1977	147	4,072,190	41	3,563,915	8	3,996,700	196	11,632,805
Acquired During 1978	712	22,699,465	23	2,882,535	7	5,116,875	742	30,698,875
Sales and Adjustments During 1978	(467)	(14,677,361)	(25)	(1,880,045)	(3)	(1,557,125)	(495)	(18,114,531)
Held at December 31, 1978	392	12,094,294	39	4,566,405	12	7,556,450	443	24,217,149
Period Held to December 31, 1978								
Less than 3 months	149	4,809,284	9	1,355,240	3	1,444,450	161	7,608,974
3 to 6 months	90	2,927,295	1	41,400	—	—	91	2,968,695
6 to 12 months	115	3,304,825	5	621,800	2	2,960,000	122	6,886,625
over 12 months	38	1,052,890	24	2,547,965	7	3,152,000	69	6,752,855
	392	12,094,294	39	4,566,405	12	7,556,450	443	24,217,149

In addition mortgages under foreclosure were held on 17 pieces of real estate for a total realizable value of $1,587,379.

Real Estate Holdings as at December 31, 1978	Single Family		Rental		Commercial Industrial		Total	
	No.	Book value	No.	Book value	No.	Book value	No.	Book Value
		$		$		$		$
Newfoundland	7	199,800	—	—	2	201,000	9	400,800
Prince Edward Island	—	—	—	—	—	—	—	—
Nova Scotia	24	522,000	2	76,500	1	725,000	27	1,323,500
New Brunswick	31	697,750	22	882,685	3	1,387,450	56	2,967,885
Quebec	83	2,741,400	11	2,360,820	2	1,408,000	96	6,510,220
Ontario	149	4,673,020	3	671,400	2	3,520,000	154	8,864,420
Manitoba	7	161,550	—	—	—	—	7	161,550
Saskatchewan	13	489,285	—	—	—	—	13	489,285
Alberta	3	154,350	—	—	1	155,000	4	309,350
British Columbia	75	2,455,139	1	575,000	1	160,000	77	3,190,139
Total	392	12,094,294	39	4,566,405	12	7,556,450	443	24,217,149

The Mortgage Insurance Company of Canada

Head Office

Suite 1200, 401 Bay Street,
Toronto, Ontario M5H 2Y4

Accounting

D. C. Toms,
Vice-President – Finance and Secretary

W. Gunsolus,
Supervisor, Accounting

Administration and Personnel

F. D. Teatro,
Director

J. W. Stewart,
Manager

G. J. Schnarr,
Assistant Manager, Administration

Miss M. E. Sparkes,
Assistant Manager,
Payroll and Personnel

Miss L. Crowder,
Supervisor, Data Processing

Business Development

C. Renaud,
Director

G. J. Pennie,
Manager and Business Development Officer (Ontario)

Claims and Real Estate

A. D. Munro,
Director

R. G. Bowden,
Manager

J. J. Traill,
Assistant Manager

Construction Inspection

E. D. Smith,
Chief Inspector

Investments

D. S. Oxley,
Investment Officer

J. E. Rohr,
Portfolio Manager

Legal

J. D. H. Bergeron,
Corporate Solicitor

Underwriting

G. W. Carpentier,
Vice-President and Chief Underwriter

C. E. Madden,
Manager, Lease Guarantee

C. E. Shoemaker,
Manager, Mortgage Insurance

A. G. Lorimer,
Assistant Manager, Lease Guarantee

Regional Offices

Halifax

P.O. Box 876, Halifax Main Post Office, Suite 722, Cogswell Tower, Scotia Square, Halifax, Nova Scotia B3J 2V9

G. S. Morgan, Manager,
F. E. Berrigan, Assistant Manager

Moncton

P.O. Box 1308, Suite 802, 860 Main Street, Moncton, New Brunswick E1C 8T6

R. A. Dryden, Manager,
F. J. Leger, Assistant Manager

Quebec

Suite 802, 1126 Chemin St-Louis, Sillery, Quebec, P.Q. G1S 1E5

A. Baron, Manager,
B. Egan, Assistant Manager

Montreal

Suite 832, 5 Place Ville Marie, Montreal, P.Q. H3B 2G2

J. D. Boudreau, Manager,
P. Sirois, Assistant Manager

Ottawa

Suite 606, 350 Sparks Street, Ottawa, Ontario K1R 7S8

S. J. Philippe, Manager,
G. J. Crepin, Assistant Manager

Toronto

P.O. Box 78, Suite 500, 401 Bay Street, Toronto, Ontario M5H 2Y4

J. G. McLean, Manager,
E. R. Weber, Assistant Manager

Hamilton

Suite 500, 155 James Street South, Hamilton, Ontario L8P 3A4

G. Russell, Manager,
D. E. Mercer, Assistant Manager

London

Suite 1102, 380 Wellington Street, London, Ontario N6A 5B5

D. R. W. Stewart, Manager,
D. G. Marry, Assistant Manager

Winnipeg

Suite 1800, 330 Portage Avenue, Bank of Montreal Building, Winnipeg, Manitoba R3C 0C4

W. M. McComb, Manager

Regina

Suite 1720, 1920 Broad Street, Regina, Saskatchewan S4P 3V2

J. C. Borland, Manager,
D. A. McDowell, Assistant Manager

Calgary

Suite 918, Sun Oil Building, 500-4th Ave. S.W., Calgary, Alberta T2P 2V6

B. K. Masterson, Manager,
M. A. Chernichan, Assistant Manager,
H. Zindler, Business Development Officer (Alberta)

Edmonton

460 Phipps McKinnon Building, 10020-101A Avenue, Edmonton, Alberta T5J 3G2

P. D. R. Smith, Manager

Vancouver

Suite 2520, 1066 West Pender St., Vancouver, B.C. V6E 3X1

K. G. Antaya, Manager,
D. R. North, Assistant Manager